Audit Report

ARMY HEALTHCARE ENTERPRISE MANAGEMENT SYSTEM

Report No. D-2001-034 January 16, 2001

Office of the Inspector General
Department of Defense

Form SF298 Citation Data

Report Date ("DD MON YYYY")	Report Type	Dates Covered (from... to) ("DD MON YYYY")
16Jan2001	N/A	

Title and Subtitle Army Healthcare Enterprise Management System	**Contract or Grant Number**
	Program Element Number
Authors	**Project Number**
	Task Number
	Work Unit Number
Performing Organization Name(s) and Address(es) OAIG-AUD (ATTN: AFTS Audit Suggestions) Inspector General, Department of Defense 400 Army Navy Drive (Room 801) Arlington, VA 22202-2884	**Performing Organization Number(s)** D-2001-034
Sponsoring/Monitoring Agency Name(s) and Address(es)	**Monitoring Agency Acronym**
	Monitoring Agency Report Number(s)

Distribution/Availability Statement
Approved for public release, distribution unlimited

Supplementary Notes

Abstract
Introduction. The audit was performed in response to allegations to the Defense Hotline concerning the procurement of the Army Healthcare Enterprise Management System. The complaint alleged that the Army Healthcare Enterprise Management System was not properly competed, potential conflicts of interest existed, and possible contract performance problems existed. The complainant also alleged that the Fort Sam Houston Information Technology Business Center, an Army organization, could have obtained better prices by using an Army blanket purchase agreement to buy the Enterprise Management System. The Information Technology Business Center provides information technology services to Fort Sam Houston tenants which include the Army Medical Command and the Army Medical Department Center and School. During FY 1999, the General Services Administration awarded three contracts with a total value of about $3.1 million for the purchase of the Enterprise Management System and consolidation of the computer servers on behalf of the Information Technology Business Center. The Enterprise Management System will provide the Information Technology Business Center with the capability to centrally manage desktop personal computers, distribute software, and inventory all systems in the local area network.

Subject Terms

Document Classification unclassified	**Classification of SF298** unclassified
Classification of Abstract unclassified	**Limitation of Abstract** unlimited
Number of Pages 35	

Additional Copies

To obtain additional copies of this audit report, visit the Inspector General, DoD Home Page at: www.dodig.osd.mil/audit/reports or contact the Secondary Reports Distribution Unit of the Audit Followup and Technical Support Directorate at (703) 604-8937 (DSN 664-8937) or fax (703) 604-8932.

Suggestions for Future Audits

To suggest ideas for or to request future audits, contact the Audit Followup and Technical Support Directorate at (703) 604-8940 (DSN 664-8940) or fax (703) 604-8932. Ideas and requests can also be mailed to:

OAIG-AUD (ATTN: AFTS Audit Suggestions)
Inspector General, Department of Defense
400 Army Navy Drive (Room 801)
Arlington, VA 22202-4704

Defense Hotline

To report fraud, waste, or abuse, contact the Defense Hotline by calling (800) 424-9098; by sending an electronic message to Hotline@dodig.osd.mil; or by writing to the Defense Hotline, The Pentagon, Washington, DC 20301-1900. The identity of each writer and caller is fully protected.

Acronyms

DFARS	Defense Federal Acquisition Regulation Supplement
DFAS	Defense Finance and Accounting Service
EMS	Enterprise Management System
FAR	Federal Acquisition Regulation
GSA	General Services Administration
ITBC	Information Technology Business Center
MHSS	Military Health Services System
MIPR	Military Interdepartmental Request
O&M	Operation and Maintenance
USC	United States Code

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

January 16, 2001

MEMORANDUM FOR AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Audit Report on Army Healthcare Enterprise Management System (Report No. D-2001-034)

We are providing this report for review and comment. We conducted the audit in response to allegations to the Defense Hotline. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The comments from the Deputy Assistant Secretary of the Army were responsive. Comments from the Deputy Surgeon General of the Army on Recommendations A.2., B.1., and B.2. were received too late to be considered in preparing the report. Therefore, if the Deputy Surgeon General of the Army does not submit additional comments by March 16, 2001, we will consider the comments received as the response to the final report.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Mr. Garold E. Stephenson at (703) 604-9332 (DSN 664-9332) (gstephenson@dodig.osd.mil) or Mr. Eric B. Edwards at (703) 604-9219 (DSN 664-9219) (eedwards@dodig.osd.mil). See Appendix D for the report distribution. The audit team members are listed inside the back cover.

David K. Steensma

David K. Steensma
Deputy Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. D-2001-034 **January 16, 2001**
(Project No. D2000CH-0108)

Army Healthcare Enterprise Management System

Executive Summary

Introduction. The audit was performed in response to allegations to the Defense Hotline concerning the procurement of the Army Healthcare Enterprise Management System. The complaint alleged that the Army Healthcare Enterprise Management System was not properly competed, potential conflicts of interest existed, and possible contract performance problems existed. The complainant also alleged that the Fort Sam Houston Information Technology Business Center, an Army organization, could have obtained better prices by using an Army blanket purchase agreement to buy the Enterprise Management System.

The Information Technology Business Center provides information technology services to Fort Sam Houston tenants which include the Army Medical Command and the Army Medical Department Center and School. During FY 1999, the General Services Administration awarded three contracts with a total value of about $3.1 million for the purchase of the Enterprise Management System and consolidation of the computer servers on behalf of the Information Technology Business Center. The Enterprise Management System will provide the Information Technology Business Center with the capability to centrally manage desktop personal computers, distribute software, and inventory all systems in the local area network.

Objectives. Our objective was to evaluate the allegations to the Defense Hotline and determine whether the Information Technology Business Center followed procurement regulations in awarding and administering the Army Healthcare Enterprise Management System contract. We also reviewed the management control program as it related to the primary audit objective.

Results. The four allegations made to the Defense Hotline were not substantiated. However, we identified issues related to planning and funding the Enterprise Management System and potential ethics violations.

The Information Technology Business Center did not appropriately fund or plan the procurement of the Enterprise Management System and a potential violation of the Antideficiency Act occurred because they used Army FY 1998 operation and maintenance funds to pay for the Enterprise Management System lease expenses in FYs 1999 and 2000. In addition, the Information Technology Business Center inappropriately used Army operation and maintenance funds instead of procurement funds to pay for a capital lease and Enterprise Management System installation costs.

The Information Technology Business Center also arranged a questionable lease agreement for the Enterprise Management System and incurred $176,112 in unnecessary finance charges and General Service Administration service costs (finding A).

Information Technology Business Center supervisors did not adequately identify and address potential ethics violations that occurred during the procurement of the Enterprise Management System. In addition, Information Technology Business Center employees were placed in a position of increased risk for potential violations of ethics laws and regulations (finding B).

The Information Technology Business Center had material management control weaknesses over planning and funding of the Enterprise Management System, interagency acquisitions, reporting of employee financial interests, and resolutions of potential conflicts of interest. See Appendix A for details on the management control program.

Summary of Recommendations. We recommend that the Army investigate and report on the potential Antideficiency Act violations arising from the Enterprise Management System contracts. We recommend that the Director, Information Technology Business Center take action to modify the Enterprise Management System contracts with appropriate lease provisions and to reduce or avoid the finance charges related to the lease payments. In addition, we recommend that the Commander, Fort Sam Houston direct the Staff Judge Advocate to investigate potential conflicts of interest and recommend appropriate administrative action, and conduct ethics training. We also recommend that the Director, Information Technology Business Center, request that the General Services Administration modify the server consolidation contract, and implement management controls over the reporting and filing of financial disclosure reports.

Management Comments. The Assistant Secretary of the Army (Financial Management and Comptroller) concurred with the recommendation to investigate and report on the potential Antideficiency Act violation. Comments from the Deputy Surgeon General of the Army on Recommendations A.2., B.1., and B.2. were received too late to be considered in preparing the report. Therefore, if the Deputy Surgeon General of the Army does not submit additional comments, we will consider the comments received as the response to the final report. See the Finding section of the report for a discussion of management comments and the Management Comments section of the report for the complete text of the comments.

Audit Response. The Assistant Secretary of the Army (Financial Management and Comptroller) comments were responsive. We request that the Deputy Surgeon General of the Army submit additional comments by March 16, 2001.

Table of Contents

Executive Summary

Introduction

Background 1
Objectives 2

Findings

A. Funding and Planning the Enterprise Management System 3
B. Financial Interests 12

Appendixes

A. Audit Process
Scope and Methodology 17
Management Control Program Review 18
Prior Coverage 19
B. Summary of Allegations and Audit Results 20
C. Funding and Leasing Criteria 22
D. Report Distribution 25

Management Comments

Assistant Secretary of the Army (Financial Management and Comptroller) 27

Background

The audit was conducted in response to allegations to the Defense Hotline that the Fort Sam Houston Information Technology Business Center (ITBC) did not effectively manage the Enterprise Management System (EMS) procurement.

ITBC Mission. The ITBC mission is to provide information support services to Fort Sam Houston and its tenants. The Army Medical Command and the Army Medical Department Center and School are major tenants on Fort Sam Houston. The ITBC provides services related to telecommunications, visual information, records management, publishing and printing, library management, and automation. The automation area encompasses computers, software, support services, and management of the data/information processing facilities. Specific ITBC automation services include:

- developing and maintaining the installation's information resources management program,
- validating and coordinating information requirements,
- developing cost estimates for the purchase of automation hardware and software applications,
- overseeing and managing the development and enforcement of security policies, and
- training installation personnel.

Enterprise Management System Project. In August 1998, the Commander, Army Medical Department Center and School, approved and funded the EMS project. The EMS project expanded rather than replaced or repaired the existing Fort Sam Houston information technology capabilities. The project consisted of leasing EMS hardware and software, and consolidating the computer servers. The EMS provided ITBC with the capability to centrally manage desktop personal computers, distribute software, and inventory all systems in the local area network. Upon completion, the EMS project will provide remote management for 4,500 desktop computers, 1,000 printers, and 75 servers. The ITBC selected the EMS made by Tivoli Systems/IBM Corporation for installation at Fort Sam Houston. Army Medical Command Policy 25-98-04, "Policy for Information Architecture Standards," August 19, 1998, established the Tivoli EMS as the standard network software. The ITBC used the General Services Administration (GSA) to contract for planning, designing, installing, and testing the EMS for the Fort Sam Houston network. The GSA awarded contracts to Software Professionals, Inc. (Software Professionals), McBride and Associates, and Dell Computer Corporation (Dell Computer). The Software Professionals contract was for the consolidation of the Fort Sam Houston servers. The Dell Computer contract was for the leasing of the servers used in the server consolidation. The McBride and Associates contract was for the installation and leasing of the EMS hardware and software. Table 1 shows the contract numbers and the total value of the contracts.

Table 1. Enterprise Management System Procurements

Contractor	Contract Number/ Delivery Order	Award Date	Contract Amount
Software Professionals	GS-35F-5404H/T0799BG0745	May 21, 1999	$ 246,829
McBride and Associates	GS-35F-4569G/T0799BG0766	June 1, 1999	2,370,900
Dell Computer	GS-35F-4076D/T0799BG0799	June 11, 1999	484,281
Total amount of contract awards			**$3,102,010**
GSA contracting fee			41,259
Total value of procurements			**$3,143,269***

* Includes unfunded FYs 2001 and 2002 lease costs totaling $961,269.

Objectives

Our objective was to evaluate four specific allegations to the Defense Hotline and determine whether the ITBC followed procurement regulations in awarding and administering the Army Healthcare Enterprise Management System contract. We also reviewed the management control program as it related to the audit objective. See Appendix A for a discussion of the audit process and the review of the management control program. See Appendix B for a discussion of the allegations to the Defense Hotline.

A. Funding and Planning the Enterprise Management System

The ITBC did not appropriately fund or effectively plan the EMS procurement. The funding for the EMS procurement was inappropriate because ITBC officials did not comply with regulations when they provided GSA $2.2 million in Army operation and maintenance (O&M) funds at the end of the fiscal year. The ineffective planning for the EMS procurement occurred because ITBC officials did not comply with policies, procedures, and regulations on:

- preparing lease purchase analysis,
- preparing funding documents, or
- documenting the EMS budget or cost estimates.

As a result, potential violations of the Antideficiency Act may have occurred because ITBC inappropriately used $2.2 million in FY 1998 O&M funds for the EMS procurement. In addition, ITBC arranged a questionable lease agreement for the EMS hardware and software, and incurred $176,112 in unnecessary finance charges and GSA service fees.

Criteria for Leasing, Interagency Acquisitions, and Antideficiency Violations

In the absence of other specific statutory authority, interagency acquisitions are governed by title 31, United States Code, section 1535 (31 U.S.C. 1535) also known as the Economy Act. Section 1501, title 31 (31 U.S.C. 1501) also plays a role by providing the standards for recording obligations of Government funds. Section 757, title 40, United States Code (40 U.S.C. 757) provides the statutory authority for the Information Technology Fund, which GSA used to award the EMS contracts. The DoD Financial Management Regulation and the General Accounting Office Principles of Federal Appropriation Law provide detailed guidance to implement those statutes. The Federal Acquisition Regulation (FAR), Defense Federal Acquisition Regulation Supplement (DFARS), and DoD Instructions provide specific guidance for DoD organizations to consider before awarding contracts for leased equipment. The DoD Financial Management Regulation and Office of Management and Budget Bulletins provide additional guidance on funding leases. See Appendix C for additional details on these laws and regulations.

EMS Funding

Army Fund Transfers. In August 1998, ITBC had unfunded requirements of $875,000 and $807,000 for the EMS and server consolidation. The Army Medical Department Center and School sent a MIPR (Military Interdepartmental

Purchase Request) to ITBC transferring $1,682,000 in FY 1998 O&M funds for the EMS and server consolidation on September 16, 1998. The Army Medical Department Center and School funded the ITBC requirements with O&M funds because procurement funds were not available. ITBC issued a MIPR transferring $1,682,000 in FY 1998 O&M funds to GSA for the server consolidation project September 23, 1998. ITBC issued a MIPR transferring an additional $500,000 in FY 1998 O&M funds to GSA for the enterprise servers on September 30, 1998. GSA accepted the MIPRs on September 25, 1998, and September 30, 1998, resulting in obligations of the funds on Army financial records.

GSA Contracting Actions. GSA awarded three delivery orders for the EMS procurements against the contracts shown in Table 1. The delivery orders had a total value of about $3.1 million and assessed service fees totaling $41,259 for GSA contracting support. A chronology of the GSA contracting actions and specific assessments are shown in Table 2.

Table 2. Chronology of GSA Contracting Actions for the EMS Procurements

Date	Event	Contractor	Amount
May 21, 1999	Delivery order T0799BG0745 awarded for server consolidation	Software Professionals	$ 246,829
June 1, 1999	Delivery order T0799BG0766 awarded for EMS installation	McBride and Associates	1,578,741
June 1, 1999	Contracting service fee assessed for EMS procurements	N/A	31,574
June 11, 1999	Delivery order T0799BG0799 awarded for leased servers	Dell Computer	295,918
June 18, 1999	Modification AC01 issued to delivery order T0799BG0799 for leased servers	Dell Computer	188,363
June 18, 1999	Contracting service fee for leased servers	N/A	9,685
March 28, 2000	Modification AS01 issued to delivery order T0799BG0766 for EMS lease costs	McBride and Associates	792,159*
	Total value of procurements		**$3,143,269**
	Less Funds provided by ITBC		2,182,000
	Total unfunded lease costs		**$ 961,269**

*$55,008 was funded with FY 1998 O&M funds and $737,151 will be funded with future year funds.

EMS Procurement Planning

Preparation of Lease Purchase Analysis. The Fort Sam Houston Installation Commander cited the Assistant Secretary of Defense (Health Affairs) policy on "Military Health Services System (MHSS) Information Technology Leasing Policy," November 12, 1997, as the authority for leasing the information technology assets, including software. The policy authorizes purchases of information technology assets if military medical readiness is not adversely impacted. The policy does not require a lease purchase analysis, however, FAR 7.4, "Equipment Lease or Purchase," states that agencies should evaluate comparative costs and other factors, when determining whether to lease or purchase equipment. DFARS 207.401, "Acquisition Considerations," states that agencies must prepare and provide the contracting officer with the justification supporting the decision to lease or purchase, if the equipment will be leased for more than 60 days. In addition, Army Regulation 25-1, "Information Management," March 25, 1997, states that the most cost-effective method for obtaining software will be used. Army Regulation 25-1 also states that a lease purchase analysis should be prepared on all acquisitions to determine the most economical way to acquire proprietary software licenses. The lease purchase analysis would have evaluated such factors as the period of use, alternative types and makes of equipment, and net purchase price. ITBC did not prepare a lease purchase analysis, or determine the most economical method of obtaining the software that DFARS 207.401 and Army Regulation 25-1 requires. A lease purchase analysis would have enabled ITBC to determine whether purchasing the EMS and servers was cost-effective and if not, provided an opportunity to request a waiver to the leasing policy.

Inspector General, DoD, Report No. 99-195, "Contract Actions for Leased Equipment," June 30, 1999, determined that the Army and other DoD organizations did not always perform (or properly perform) required lease purchase analyses before awarding contracts for leased equipment. The deficiencies identified in Report No. 99-195 occurred on contracting actions from October 1, 1995 through February 28, 1997. In response to recommendations in that report, the Deputy Assistant Secretary of the Army (Procurement) issued a memorandum August 12, 1999. The memorandum reminded Army contracting officers to review the lease purchase analyses before awarding any new contracts or extending existing contracts for leased equipment. Accordingly, we are not recommending that the Army take additional corrective action as a result of this audit. Army contracting officers are required to review the lease purchase analysis, so the guidance in the memorandum should provide sufficient control for leasing actions on interagency acquisitions.

Funding Documents. ITBC arranged for GSA to award the EMS and server consolidation contracts using the GSA Information Technology Fund. ITBC officials chose to use GSA contracting services instead of an Army contracting office for the EMS procurement. ITBC officials stated that they used GSA because O&M funds could be converted to multiyear funds by using the GSA Information Technology Fund. Also, GSA customers could record valid obligations of funds when executing an interagency agreement if there was a

bona fide need for the products or services, within the scope of the interagency agreement. The funds were available for the entire period of performance, even if such performance crossed fiscal years.

On June 1, 1995, the Army Medical Command established a memorandum of understanding with GSA for Federal information support services. The memorandum of understanding states that the GSA Technical Support Division will provide information processing services to the Army through delivery orders issued to contractors. The memorandum of understanding requires the Army to comply with its own procurement regulations and policies. The memorandum of understanding also requires funding documents to ". . . cite the amount being obligated by the client (including GSA surcharge) and will describe the project(s) and the agency requirement that will be met by the project(s)." The Defense Finance and Accounting Service Regulation (DFAS) 37-1, "Finance and Accounting Policy Implementation," provides specific instructions for completing MIPRs. The DFAS instruction requires agencies to enter a description for each type of work/service requested. In addition, DFAS 37-1 provides a sample of a completed MIPR with a detailed description of the work/services requested.

ITBC used the MIPRs to provide GSA funds for the EMS and the server consolidation projects. The ITBC MIPR submissions did not comply with the memorandum of understanding or DFAS Regulation 37-1. The ITBC MIPRs, and their acceptance by GSA, lacked essential details to determine whether the MIPRs were issued or accepted under 40 U.S.C. 757 (Information Technology Fund) or the memorandum of understanding. In addition, ITBC did not describe the EMS or server consolidation projects on the MIPRs or provide specific information that GSA needed to determine the scope of the work or services that ITBC was requesting.

Information Management Project Document. The ITBC director approved the EMS because the capability of ITBC to monitor and repair the automation equipment attached to the Fort Sam Houston network was limited. The ITBC director issued a memorandum formally approving the EMS project on July 28, 1998. The memorandum states that the approval became invalid on September 30, 1998, ". . . if the equipment and/or service has not been procured or is not in the process of being procured." The EMS project document accompanying the memorandum did not contain essential information such as acquisition cost, type of funds, number of client workstations and servers, and the annual maintenance costs. Army Regulation 25-1 states that the information management requirement/project document (DA Form 5695) is a life cycle management document used to identify, document, and justify requirements for information management systems that exceed $100,000.

EMS Independent Cost Estimate. ITBC did not prepare a cost estimate for the EMS and server consolidation that documented the least expensive acquisition method. DoD Instruction 7041.3, "Economic Analysis for Decisionmaking," November 7, 1995, and Army Regulation 11-18, "The Cost and Economic Analysis Program," January 31, 1995, require Army organizations to prepare a comparative cost analysis to show that the lowest cost method of acquisition has been considered as the least expensive life-cycle cost

to the Government. ITBC provided GSA with cost estimates of $1.6 million and $600,000 for the estimated procurement cost of the EMS and server consolidation. However, the $1.6 million cost estimate for the EMS was about $800,000 less than the actual contract cost of about $2.4 million. The server consolidation cost estimate of $600,000 was about $140,795 less than the actual contract costs of $740,795. The "Army Economic Analysis Manual," June 1995, states that the documentation for a cost estimate must provide an audit trail which includes the computations and methodologies used to develop the estimate. ITBC officials did not document their cost estimates and were unable to fully explain the large discrepancies in the estimates. The ITBC Business Systems Solutions Division Chief (division chief) stated that the $1.6 million cost estimate did not include labor for the EMS installation.

Compliance with Financial Laws and Regulations

Recording Obligations. ITBC officials provided us with documentation from GSA to support the obligation of the $2.2 million in O&M funds at the end of FY 1998. The GSA documentation states that a customer with an interagency agreement may use the Information Technology Fund to record an obligation without a contract or task order in place if GSA has accepted the funds. However, we find no specific language in 40 U.S.C. 757 that allows a customer of the fund to "bank" expired funds for contracts in subsequent periods. ITBC may have violated the Antideficiency Act by using $2.2 million in FY 1998 O&M funds to pay for the installation and leasing of the EMS and servers in FYs 1999 and 2000. ITBC may have also violated the Antideficiency Act by inappropriately using O&M funds instead of Army procurement funds to pay for a capital lease and EMS installation costs.

Bona Fide Need. ITBC did not establish that a bona fide need existed in FY 1998 for the EMS or the server consolidation. Of the $2.2 million in FY 1998 O&M funds that ITBC sent to GSA, about $691,592 was used for leased payments in FYs 1999 and 2000. The remaining $1.5 million was for labor, travel, and other direct costs for the installation of the EMS and the server consolidation. The bona fide need rule applies to Economy Act orders or orders issued under other statutes. Agencies requesting property or services must show a legitimate need in the fiscal year of the appropriation in order to apply the bona fide need rule. O&M funds are annual appropriations that agencies cannot use for future needs after expiration of the funds. The General Accounting Office Appropriation Law, volume 1, chapter 5, states ". . . if deliveries are scheduled only for a subsequent fiscal year, or if contract timing effectively precludes delivery until the following fiscal year, it will be presumed that the contract was made in the earlier fiscal year to obligate funds from an expiring appropriation and that the goods or materials were not intended to meet a bona fide need of that year." In general, services that are continuing and recurring in nature are severable and the services must be charged to the fiscal year in which they are rendered. ITBC lack of planning in FY 1998, and the fact that GSA awarded the EMS contracts 8 months after the expiration of the O&M funds, indicate that the EMS project was not a FY 1998 requirement. In addition, the ITBC lease agreements met the definition of recurring services that are severable between fiscal years. The ITBC lease agreements for the server

consolidation and EMS hardware were for a 36-month period from July 1, 1999 to June 30, 2002. The ITBC lease agreement for the EMS software covered the period from December 1, 1999 to November 30, 2002.

Another indication that ITBC did not have a bona fide need in FY 1998 for the EMS was that the MIPRs ITBC sent to GSA did not meet the requirements outlined in 31 U.S.C. 1501, DFAS Regulation 37-1, or the memorandum of understanding. Section 1501(a)(1), title 31, requires that agencies have documentary evidence of a binding agreement for specific goods or services before recording a valid obligation. The memorandum of understanding between GSA and the Army Medical Command requires that funding documents provide a description of the projects. The ITBC MIPRs provided to GSA indicated "The list of items to be leased and/or purchased will be sent at a later date." A handwritten note in parentheses on the MIPRs states, "server consolidation for EMS." ITBC officials maintained that the MIPRs clearly indicated to GSA that the funds were for the EMS server consolidation.

We disagree that the ITBC MIPRs identified specific goods and services. ITBC identified EMS and server consolidation as two separate projects. The phrase "server consolidation for EMS" does not describe either project. The EMS was a complicated project involving designing, installing, and testing the EMS hardware and software on 4,500 computers and 1,000 network printers. In addition, the EMS contractor was to provide classroom and on-the-job training for ITBC personnel. The server consolidation involved leasing and installing 75 servers. ITBC did not provide GSA the statement of work with the details of the EMS and server consolidation projects until January 14, 1999.

Funding of Capital Leases. ITBC did not comply with 31 U.S.C. 1301 and a potential violation of the Antideficiency Act occurred by using O&M funds to fund a capital lease on the McBride and Associates contract. Procurement funds must be used for capital leases and O&M funds are used for operating leases. Of the $691,592 total lease payments, ITBC used approximately $310,882 for the EMS software lease. The present value of the EMS software lease payments could not exceed 90 percent of the assets' fair value to qualify as an operating lease. See Appendix C for a discussion of the criteria related to capital leases funding.

In response to our inquiries, ITBC prepared an economic analysis that calculated the present value of $971,907 for lease payments over 3 years totaling $1,064,664 for the EMS software. ITBC used the EMS software prices in effect on GSA contract GS35F-4984H with International Business Machines in May 1999 to determine the fair market value. ITBC determined that the GSA schedule price for the EMS software was $1,231,432. ITBC stated that IBM informed them ". . . for a $1.2 million order, an agency could reasonably expect to negotiate a 5-10 percent discount under the contract." ITBC used a 10 percent discounted price of $1,108,289 because we questioned their use of the $1,231,432 fair market value in their present value calculation. Contract GS35F-4984H limited customer orders to a maximum value of $500,000. The contract states that the maximum order threshold ". . . represents the point where it is advantageous for the ordering office to seek a price reduction"

directly from the contractor. ITBC concluded that the EMS software lease was an operating lease based on a present value of $971,907 that was 88 percent of the fair market value ($1,108,289).

We disagree that the EMS software lease was an operating lease. GSA and McBride and Associates provided us documentation that showed total EMS software lease payments of $1,100,619. The total software lease payments of $1,100,619 result in a present value of $1,004,729 or 91 percent of the ITBC fair market value ($1,108,289). We concluded that the EMS software lease was a capital lease that required procurement funds. We also disagree that ITBC could only obtain a 10 percent discount off the GSA schedules. In FY 1999, the Army Communications-Electronics Command demonstrated that substantial discounts were obtainable from GSA schedules. The Command negotiated four agreements for various information technology products and services ranging from 42 percent to 64 percent off the GSA schedules. The Command also negotiated a customer agreement for the purchase of EMS software that offered discounts from the GSA price schedule. The Army awarded the blanket purchase agreement 1 month after the McBride and Associates contract award. The EMS cost, using the blanket purchase agreement prices, was $968,561 or about 21 percent less than the GSA schedule price. We believe that the $968,561 represents a more accurate estimate of the fair market value. The Statement of Federal Financial Accounting Standards No. 6, "Accounting for Property, Plant, and Equipment," June 1996, stated that fair market value is the price for which an asset could be bought or sold in an arm's-length transaction between unrelated parties (for example, between a willing buyer and a willing seller). The $968,561 was the result of Army Communications-Electronics Command negotiations for EMS software prices.

Funding Installation Costs. ITBC used O&M funds for about $1.0 million in EMS installation costs on the McBride and Associates contract, and $246,829 for the installation of leased servers on the Software Professional contract. The $1.0 million and $246,829 installation costs were primarily labor costs of McBride and Associates and Software Professionals, respectively. In general, investments exceeding $100,000 are capital assets that should be funded with procurement funds. DoD Financial Management Regulation, volume 2A, provides the criteria for determining whether an item is an expense or an investment. The Financial Management Regulation states that the labor of contractor personnel included in the production or construction of a capital asset shall be classified as an investment cost.

EMS Lease Agreement

Lease Documentation. As a result of inadequate planning, ITBC initiated a questionable lease agreement and maintained insufficient controls over leased assets. A GSA official informed ITBC that the statement of work on the McBride and Associates and Software Professionals contracts constituted the lease agreements. The GSA official stated that GSA was not involved in the vendors' internal leases process. The statement of work did not address an EMS software lease, or identify lease payments or disposition of leased assets. ITBC was unable to adequately describe the lease terms for the EMS software.

In response to our inquiries concerning the EMS software lease, McBride and Associates informed GSA in a letter dated May 16, 2000, that when the lease expires, the Government could return the leased products or extend the lease for $25,000 per year. McBride and Associates stated that Systems Finance Corporation was the lessor for the EMS hardware and software. We believe that GSA should modify delivery order T0799BG0766 to McBride and Associates to include the monthly lease cost and the options at the end of the EMS leases.

Lease Costs. The EMS software lease was not cost-effective. ITBC incurred additional finance charges of $172,659 for leasing the EMS software and $3,453 in GSA service fees. In addition, ITBC must either extend the lease for $25,000 per year or obtain (through lease or purchase) a new EMS at the end of the 36 month lease. Furthermore, ITBC incrementally funded the last 2 years of the EMS software lease thereby increasing the Army risk of losing leased assets if funding is not available.

Recommendations and Management Comments

A.1. We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller):

a. Investigate delivery order T0799BG0766 on contract GS-35F-4569G, delivery order T0799BG0799 on contract GS-35F-4076D, and delivery order TO799BG0745 on contract GS-35F-5404H for potential Antideficiency Act violations arising from the use of Army FY 1998 operation and maintenance funds to pay for EMS lease expenses in FYs 1999 and 2000 and the improper funding of a capital lease and labor costs for installation of a capital asset.

b. Comply with the reporting requirement in DoD Financial Management Regulation 7000-14-R, volume 14, "Administrative Control of Funds and Antideficiency Act Violations," if any violations of the Antideficiency Act occurred,

c. Provide a copy of the preliminary review report, the monthly status report on the formal investigation, and the final formal investigation report to the Inspector General, DoD.

Army Comments. The Assistant Secretary of the Army (Financial Management and Comptroller) concurred with the recommendation. On October 24, 2000, the Assistant Secretary directed the Commander, Army Medical Command to investigate the potential Antideficiency Act violation on the EMS contracts and to prepare the required reports. The Assistant Secretary also stated that the preliminary report would be forwarded to the Inspector General, DoD.

A.2. We recommend that the Director, Information Technology Business Center:

a. Request that the General Services Administration modify delivery order T0799BG0766 on contract GS-35F-4569G to include monthly lease payments and Government options at the end of the lease.

b. Determine whether the $172,659 in finance charges and $3,453 in General Service Administration service fees can be reduced or avoided through a lump sum payment on delivery order T0799BG0766 on contract GS-35F-4569G and provide the funds, if available, to the General Service Administration.

c. Use Army procurement funds for the unfunded increments of the Enterprise Management System software lease.

Management Comments Required. Comments on the draft report were received from the Deputy Surgeon General of the Army too late to be incorporated into the final report. Therefore, if the Deputy Surgeon General does not submit additional comments, we will consider those comments as the management response to the final report.

B. Financial Interests

ITBC supervisors did not adequately identify and address potential conflicting financial interests that occurred during the procurement phase of the Enterprise Management System (EMS). Specifically, ITBC supervisors did not:

- consult Army ethics counselors about a potential conflict of interest issue;
- conduct adequate reviews of financial disclosure reports; or
- update position descriptions to include a requirement to file financial disclosure reports.

The situation occurred because ITBC supervisors consulted GSA contracting officials instead of an Army ethics counselor to resolve a potential conflict of interest issue. In addition, ITBC supervisors did not comply with instructions from the Staff Judge Advocate and the DoD Joint Ethics Regulation for reviewing financial disclosure reports or updating employee position descriptions. The inadequate response of ITBC supervisors prevented the Army from preserving the integrity of the procurement process by identifying and resolving potential conflicts of interest at the earliest possible moment. In addition, ITBC employees were placed in a position of increased risk for violating the procurement integrity laws and regulations, which could result in administrative and criminal penalties.

DoD Ethics Regulation

DoD 5500.7-R, "Joint Ethics Regulation," August 30, 1993, provides guidance to DoD employees and military personnel on standards of ethical conduct and ethics guidance, including direction in the areas of financial and employment disclosure systems, post-employment rules, enforcement, and training. The regulation implements various public laws and Executive Orders on ethical conduct of Government personnel. Violations of the standards of ethical conduct can result in criminal prosecution or adverse personnel actions.

Resolving Conflicts of Interest. DoD 5500.7-R states that the resolution of actual or apparent conflicts of interest is the responsibility of the DoD Component command or organization. The responsible individual should consult with an ethics counselor about alternatives for resolution of any conflicts of interest. A supervisor who receives a report of a suspected conflict of interest or violation should promptly report the matter to an ethics counselor. The supervisor may act only after consultation with the local ethics counselor.

Financial Disclosure Reports. FAR 3.104-3, "Definitions," states that an individual participates "personally and substantially" in a procurement, if they are actively involved in the preparation of statement of work, evaluation of bids or proposals, or selecting a source. DoD 5500.7-R requires DoD employees with official responsibilities that require them to participate personally and substantially in decisions, or exercise significant judgment in taking an official action for contracting or procurement, to file a financial disclosure report. The individual should submit an annual financial disclosure report through their supervisor to an ethics counselor by November 30. The financial disclosure report covers the individual's financial information such as assets and income, liabilities, and outside positions for the preceding 12 months. The supervisor is responsible for ensuring that the financial disclosure report is complete and that no interest or position violates or appears to violate applicable ethics laws and regulations.

Position Descriptions. DoD 5500.7-R requires personnel offices to coordinate with ethics counselors and supervisors to ensure that position descriptions include a statement regarding the submission of a financial disclosure report. As positions are modified, combined, or added, the duties of each position must be reviewed to determine whether a financial disclosure report is required.

Responsibility for Ethics Program Guidance

The Staff Judge Advocate is responsible for the ethics program at Fort Sam Houston. Specifically, the Staff Judge Advocate provides the organizations at Fort Sam Houston with ethics counselors, ethics training, and instructions on financial disclosure reports. The ethics counselors assist in implementing and administering the organization's ethics program and provides ethics advice to DoD employees and supervisors. In addition, the Staff Judge Advocate conducts annual ethics training for the supervisors and employees at Fort Sam Houston.

The Staff Judge Advocate at Fort Sam Houston provided instructions on financial disclosure reports that included responsibilities for employees and supervisors. On September 1, 1999, the Staff Judge Advocate issued a memorandum that provided instructions for the annual financial disclosure reports. The memorandum states that supervisors are responsible for reviewing the financial disclosure reports for completeness and possible conflicts of interest. The memorandum also states that supervisors are responsible for determining which employees within their organization are required to file financial disclosure reports. The memorandum provided a list of employees filing financial disclosure reports the previous year to assist the ITBC supervisors with their determinations. The memorandum also states that as employee positions are changed, added, or deleted, supervisors must review the position against the standards for filing financial disclosure reports. The guidance further requests supervisors to keep the Staff Judge Advocate informed of any changes in the employees required to file financial disclosure reports.

ITBC Management Oversight

The ITBC director and the division chief did not adequately address a potential conflict of interest during the EMS procurement. Also, the ITBC supervisors did not ensure that employees' financial disclosure reports were accurate or that position descriptions included the requirement for filing financial disclosure reports.

Potential Conflict of Interest. In December 1998, an ITBC employee informed the division chief that their spouse worked for a partner/subcontractor of Software Professionals, a potential bidder for the EMS contract. The division chief allowed the ITBC employee to participate in the EMS procurement after the employee informed him of a potential conflict of interest. The division chief did not notify an Army ethics counselor of the potential conflict of interest, or determine whether the employee had an actual conflict of interest, or the appearance of conflict of interest. Further, the division chief did not document that any action was taken to mitigate or address the employee's conflict of interest or why the employee continued to participate in the EMS procurement. The division chief stated that he advised GSA of the potential conflict of interest, and a GSA contracting official advised him that a conflict of interest did not exist because there was no contract with the company. The division chief relied on GSA because GSA was awarding the EMS contract for ITBC.

Subsequently, the division chief assigned the employee to review the technical proposals with each contractor's name and costs removed. The purpose of the review was to ensure that the EMS technical review team had covered the important points in their analysis. The employee also attended two meetings with Software Professionals. The employee participated in a site visit by Software Professionals before the contract award on March 10, 1999, and the May 18, 1999, "kick-off" meeting after the contract award. The employee and the employee's spouse were present at the "kick-off" meeting. The division chief removed the employee as the client representative for the Software Professionals contract after the kick-off meeting on May 19, 1999. The client representative also acts as the contracting officer technical representative by reviewing and evaluating the contractor's technical performance, advising GSA of any problems affecting delivery or costs of completed work, and inspecting contract deliverables. However, the appearance of a conflict of interest still existed after the division chief removed the employee because the Software Professionals' contract continued to show the ITBC employee as the client representative. We believe that the contract should be modified to remove the ITBC employee's name as client representative and that the Staff Judge Advocate should review the actions of the ITBC supervisor and recommend any additional actions, as appropriate.

Supervisory Review of Financial Disclosure Reports. The ITBC director and division chief did not adequately review financial disclosure reports as required by DoD 5500.7-R and the Staff Judge Advocate's September 1, 1999 instructions. The FY 1999 financial disclosure reports for two ITBC employees involved in the EMS procurement did not show that their spouses received salaries from Defense contractors. The employees' omission of the spouses' salaries from the financial

disclosure reports did not appear to be intentional. The two employees had never previously filed financial disclosure reports and may not have fully understood the reporting requirements. However, both employees had previously provided written statements informing their supervisors of the potential conflicts of interest involving their spouses' employment. One ITBC employee's spouse was a contractor employee working as the ITBC site manager that reported directly to the ITBC director from October 1, 1997, through December 8, 1999. The ITBC director approved the financial disclosure report for the ITBC employee. The ITBC director and the division chief approved the financial disclosure reports without questioning the omitted salaries or referring the matter to an ethics counselor. In 1998 and 1999 the ITBC director and division chief attended ethics training that included conflicts of interest, gifts, official travel, and post-Government employment. We believe that the ITBC supervisors should have additional ethics training with emphasis on documenting, reporting, and resolving conflicts of interest, and reviewing financial disclosure reports.

Employee Position Descriptions. ITBC management did not include the requirement for filing financial disclosure reports in five position descriptions as required by DoD 5500.7-R. The deficient position descriptions were those of the Enterprise Management Division Chief, EMS Project Manager, and three members of the EMS technical review panel. The five employees performed duties related to the EMS procurement that met the FAR 3.104-3 definition of personal and substantial participation in a procurement action. In addition to the actual duties performed on the EMS procurement, the position descriptions for four of the five employees contained duties that required filing a financial disclosure report. For example, one position description included a requirement to review contract proposals and serve as a contracting officer's representative. Although three of the employees filed financial disclosure reports for FY 1999, ITBC needs to ensure that the position descriptions include a requirement to file a financial disclosure report. The position descriptions are a management tool that enables an organization to identify employees required to file financial disclosure reports and to ensure that annual reporting requirements are met. Consequently, ITBC needs to review each position description and, if appropriate, include a requirement to file a financial disclosure report. In addition, the Staff Judge Advocate should have a complete list of all ITBC employees required to file financial reports to ensure that the annual reporting requirements are completed.

Recommendations and Management Comments

B.1. We recommend that the Commander, Fort Sam Houston direct the Staff Judge Advocate to:

a. Review the potential conflict of interest on the Enterprise Management System procurement and recommend administrative action, as appropriate.

b. Provide ethics training to all Information Technology Business Center supervisors on documenting, reporting, and resolving conflicts of interest, and reviewing financial disclosure reports.

B.2. We recommend that the Director, Fort Sam Houston Information Technology Business Center:

a. Review the position descriptions for all Information Technology Business Center employees and identify those positions that meet the requirements in Federal Acquisition Regulation 3.104-3 for participating personally and substantially in Government procurements.

b. Request that the General Services Administration modify the Software Professionals contract to change the Information Technology Business Center client representative.

c. Modify appropriate position descriptions to include a requirement to file a financial disclosure report.

d. Update the list of Information Technology Business Center employees required to file financial disclosure reports that is maintained by the Staff Judge Advocate, Fort Sam Houston.

Management Comments Required. Comments on the draft report were received from the Deputy Surgeon General too late to be incorporated into the final report. Therefore, if the Deputy Surgeon General does not submit additional comments, we will consider those comments as the management response to the final report.

Appendix A. Audit Process

Scope and Methodology

Work Performed. To evaluate the validity of the allegations, we reviewed the ITBC procedures for awarding and administering the Army Health Care Enterprise Management System contract. We reviewed the 1998 and 1999 financial disclosure reports and position descriptions for ITBC employees involved in the EMS procurement. We also reviewed the steps that ITBC supervisors took to report and resolve a potential conflict of interest. We reviewed the prices for the EMS software on the McBride and Associates contract and the Army blanket purchase agreement negotiated by the Army Communications-Electronics Command. The contract documentation that we reviewed included solicitations, statements-of-work, contractor price proposals, MIPRs, and GSA and contractor correspondence. We interviewed officials from the Army Medical Command, Army Communications-Electronics Command, ITBC, GSA, contractors, and the complainant.

DoD-Wide Corporate Level Government Performance and Results Act Coverage. In response to the Government Performance Results Act, the Secretary of Defense annually establishes DoD-wide corporate level goals, subordinate performance goals, and performance measures. This report pertains to achievement of the following goal, subordinate performance goal, and performance measure.

> **FY 2001 DoD Corporate Level Goal 2:** Prepare now for an uncertain future by pursuing a focused modernization effort that maintains U.S. qualitative superiority in key warfighting capabilities. Transform the force by exploiting the Revolution in Military Affairs, and reengineer the Department to achieve a 21st century infrastructure. **(01-DoD-2) FY 2001 Subordinate Performance Goal (2.3):** Streamline the DoD infrastructure by redesigning the Department's support structure and pursuing business practice reforms. **(01-DoD-2.3) FY 2001 Performance Measure 2.3.1:** Percentage of the DoD Budget Spent on Infrastructure. **(01-DoD-2.3.1)**

DoD Functional Area Reform Goals. Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following objective and goal in the Information Technology Management Functional Area:

> **Objective:** Provide services that satisfy customer information needs.
> **Goal:** Upgrade technology base. **(ITM-2.3)**

General Accounting Office High-Risk Area. The General Accounting Office has identified several high-risk areas in the DoD. This report provides coverage of the Defense Contract Management high-risk area.

Use of Computer-Processed Data. We did not rely on computer-processed data during the audit.

Use of Technical Assistance. We obtained legal assistance from the Office of General Counsel, DoD, concerning ITBC compliance with laws and regulations related to the potential Antideficiency Act violations, adequacy of the lease agreements, and the potential conflicts of interest.

Audit Type, Dates, and Standards. We performed this economy and efficiency audit from February 2000 through July 2000 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, we included tests of the management controls that we deemed necessary.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD and the GSA. Further details are available upon request.

Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program, August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of Review of Management Control Program. We reviewed the adequacy of management controls over the process that ITBC used to plan and award the Army Healthcare EMS contract. Specifically, we examined management controls over compliance with laws and regulations for funding and leasing information technology systems. In addition, we examined management controls to ensure that ITBC complied with ethics regulations. We also reviewed the adequacy of the self-evaluation of the management control program at ITBC.

Adequacy of Management Controls. We identified material management control weaknesses, as identified by DoD Instruction 5010.40. ITBC had not implemented adequate management controls to ensure that a valid lease purchase analysis and other planning documents were prepared to support the type and amount of funding for the EMS procurement or that interagency acquisitions complied with statutory and regulatory requirements. In addition, ITBC did not have adequate management controls to report and resolve potential conflicts of interest. Recommendations A.1., A.2., B.1., and B.2., if implemented, will assist in correcting the cited weaknesses. Also, guidance issued by the Deputy Assistant Secretary of the Army (Procurement) on August 12, 1999, should improve the controls over lease purchase analyses for acquisitions. A copy of the report will be provided to the senior official responsible for management controls in the Army.

Adequacy of Management's Self-Evaluation. ITBC officials did not identify funding and leasing of information technology systems or ethics regulations

compliance as assessable units and, therefore, did not identify or report the material management control weaknesses identified by the audit.

Prior Coverage

Inspector General, DoD, Report No. 99-195, "Contract Actions for Leased Equipment," June 30, 1999

Appendix B. Summary of Allegations and Audit Results

Allegation 1. The prices for the EMS on the ITBC contract were higher than the prices on a blanket purchase agreement that the Army Communications-Electronics Command negotiated on behalf of the Army Small Computer Program Office.

Audit Results. The implication that ITBC could have saved funds by using the Army blanket purchase agreement to obtain the Tivoli EMS was not substantiated. The ITBC could not have used the Army blanket purchase agreement because the agreement was not finalized until June 30, 1999, or one month after the ITBC contract. In addition, Communications-Electronics Command officials stated that ITBC would not have been aware of the pending Army blanket purchase agreement. However, ITBC would have realized substantial savings if the Army blanket purchase agreement had been available for use. Finding A discusses the differences in price between the ITBC contract and the Army blanket purchase agreement.

Allegation 2. ITBC employees directed the selection of the Tivoli EMS because of outside business interests with Tivoli employees.

Audit Results. The allegation was not substantiated. The ITBC selected the Tivoli EMS because the Army Medical Command, Policy 25-98-04, "Policy for Information Architecture Standards," August 19, 1998, established the Tivoli EMS as the standard networking software, and this decision was supported by the work of a Technical Integration Working Group chartered by the Assistant Secretary of Defense for Health Affairs. We found no evidence that ITBC personnel participated in the study leading to the decision to select the Tivoli EMS as the standard. However, we identified a potential conflict of interest involving one ITBC employee participating in the EMS procurement. We also identified management control weaknesses in the filing, preparation, and review of financial disclosure reports for ITBC employees. Finding B addresses the potential conflicts of interest and the management control weaknesses related to the financial disclosure reports.

Allegation 3. The EMS contract was not properly competed and "high level" officers questioned why the contract was a sole-source procurement.

Audit Results. The allegation was not substantiated. The EMS solicitation required the winning contractor to lease and install the hardware and software for the Tivoli EMS. As discussed in the audit response to Allegation 2, ITBC selected Tivoli because it was the standard networking software for the Army Medical Command. In addition, ITBC officials showed that they reviewed EMS software of Computer Associates, Hewlett-Packard Company, and Platinum Technology. The ITBC concluded that these EMS packages did not provide the features and complexity comparable to the Tivoli EMS. The GSA awarded three contracts (EMS software and server consolidation) using competitive contracting

procedures. The GSA received four contractor price proposals and selected the winning contractor based on technical capability, past performance, delivery terms, and prices.

Allegation 4. The EMS contractor had not made adequate progress on the contract.

Audit Results. The allegation was not substantiated. The contract performance period was June 1, 1999, to December 31, 1999. On February 29, 2000, the ITBC signed the acceptance certificate for the contract with McBride and Associates. The acceptance certificate stated that McBride and Associates had delivered and installed all the equipment required by the contract. The acceptance certificate also stated that the Government had inspected and tested all the equipment.

Appendix C. Funding and Leasing Criteria

United States Code

Section 1501, title 31, United States Code, establishes minimum requirements for recording obligations for contracts. Specifically, for an agency to record a valid obligation, there must be documented evidence of an executed written agreement between agencies before the obligation of the appropriation or funds expires. The funds must be used for specific goods or services to be leased or purchased. This requirement applies to all interagency transactions.

The Economy Act specifically dictates the authority for voluntary interagency agreements and governs such transactions in the absence of other, specific statutory authority. An Economy Act agreement must meet the requirements of 31 U.S.C. section 1501(a)(1) with one additional requirement. Funds transferred under an Economy Act agreement may not exceed the period of availability of the source appropriation, if the performing agency has not performed or incurred valid obligations under the agreement.

Section 1501, title 31, United States Code directs that an amount shall be recorded as an obligation only when supported by documentary evidence of a binding agreement between an agency and another person or agency. The use of inappropriate funds for capital leases would initially constitute a violation of the "purpose statute," 31 U.S.C. 1301(a). If the acquiring command is unable to make adjustments to fund the acquisition from the correct appropriation, then an Antideficiency Act violation may occur, either at section 1341(a)(1)(A) or 1517(a), title 31, United States Code. Those sections of the code prohibit expenditures and obligations exceeding the amount available in appropriations or administrative subdivisions of appropriations, respectively.

Section 757, title 40, United States Code (40 U.S.C. 757) establishes the Information Technology Fund by specifying the content, costs, and capital requirements for the Information Technology Fund. The purpose of the Information Technology Fund is to provide information technology hardware, software, or services using multiyear contracts. The statute also provides that the funds obligated against the Information Technology Fund are available without fiscal year limitations.

Lease Purchase Analysis Guidance

Federal Acquisition Regulation 7.4, "Equipment Lease or Purchase," states that agencies must evaluate comparative costs and other factors, when determining whether to lease or purchase equipment, on a case-by-case basis. Agencies should consider some of the following factors: financial advantages, cumulative rental payments, and service costs.

Defense Acquisition Regulation Supplement 207.4, "Equipment Lease or Purchase," mandates that requiring organizations prepare and provide contracting officers with justifications that support the decision to lease versus purchase equipment, if the equipment will be leased more than 60 days. The supplement also states that capital leases are essentially installment purchases of property, therefore, agencies must use procurement funds for capital leases.

DoD Instruction 7041.3, "Economic Analysis for Decisionmaking," November 7, 1995, requires agencies to prepare a comparative cost analysis to show that the lowest cost method of acquisition has been considered at the least expensive life-cycle cost to the Government.

Capital Lease Funding Guidance

Office of Management and Budget Bulletin No. 91-02, "Instructions on an October Update of the Baseline; Treatment of Purchases, Lease-Purchases, and Leases and Presentation of Credit Data in the FY 1992 Budget," October 18, 1990, provides the criteria for operating and capital leases. Bulletin No. 91-02 was updated by Office of Management and Budget Circular A-11, part 3, "Planning, Budgeting, and Acquisition of Capital Assets," July 12, 1999, however, the guidance on operating and capital leases did not change. The criteria defines a capital lease as any lease other than a lease-purchase (that is an asset transferred to the Government at the end of the lease term) that does not meet the criteria of an operating lease. An operating lease must meet all of the criteria shown in the following bulleted sentences. If the criteria is not met, the lease will be considered a capital lease or a lease-purchase, as appropriate.

- Ownership of the asset remains with the lessor during the term of the lease and is not transferred to the Government at or shortly after the end of the lease term.

- The lease does not contain a bargain-price purchase option.

- All risks of ownership of the asset remain with the lessor, unless the Government is at fault for such losses.

- The lease term does not exceed 75 percent of the estimated economic life of the asset.

- The present value of the minimum lease payments over the life of the lease does not exceed 90 percent of the fair market value of the asset at the inception of the lease.

- The asset is a general purpose asset rather than a special purpose asset of the Government, and is not built to the unique specification of the Government as lessee.

- There is a private sector market for the asset.
- The asset is not constructed on Government land.

DoD Financial Management Regulations

DoD Financial Management Regulation 7000.14-R, volume 4, chapter 7, section 070207 implements the capital lease rules in Office of Management and Budget Bulletin No. 91-02.

DoD Financial Management Regulation 7000.14-R, volume 2A, chapter 1 states that O&M funds are used for expenses incurred to operate and maintain the organization. Investments are defined as costs resulting in the acquisition of, or an addition to, end items, and are budgeted with procurement or military construction funds. In general, an item with a unit cost exceeding $100,000 is considered an investment. A contractor's labor cost incurred for the production or the construction is included in determining the cost of an investment.

DoD Financial Management Regulation 7000.14-R, volume 14, chapters 2 through 10 addresses Antideficiency Act violations. Specifically, chapter 2 addresses the types of Antideficiency Act violations and provides examples of the various violations. Chapters 3 through 10 provide requirements for conducting investigations of potential Antideficiency Act violations and reporting the results of the investigations.

Principles of Federal Appropriations Law

General Accounting Office Appropriation Law, volume 1, chapters 4 and 5, discusses the purpose for which appropriated funds may be used, and the time limits within which they may be obligated and expended. Volume 2, chapter 7, discusses obligations including the criteria for recording obligations, the specificity requirement and interagency transactions.

Appendix D. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller/Chief Financial Officer)
  Deputy Chief Financial Officer
  Deputy Comptroller (Program/Budget)

Department of the Army

Assistant Secretary of the Army (Financial Management and Comptroller)
Auditor General, Department of the Army
Commander, Army Medical Command
Commander, Army Medical Department Center and School
Commander, Fort Sam Houston
Director, Information Technology Business Center

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Department of the Air Force

Non-Defense Federal Organizations and Individuals

Office of Management and Budget
General Services Administration

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Management, Information, and Technology, Committee on Government Reform
House Subcommittee on National Security, Veterans Affairs, and International Relations, Committee on Government Reform

Assistant Secretary of the Army (Financial Management and Comptroller) Comments

DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY
FINANCIAL MANAGEMENT AND COMPTROLLER
109 ARMY PENTAGON
WASHINGTON DC 20310-0109

REPLY TO ATTENTION OF

November 29, 2000

MEMORANDUM FOR THE DIRECTOR, CONTRACT MANAGEMENT DIRECTORATE, OFFICE OF THE ASSISTANT INSPECTOR GENERAL FOR AUDITING, DEPARTMENT OF DEFENSE, 400 ARMY NAVY DRIVE (ROOM 801), ARLINGTON, VA 22202-2284

SUBJECT: Draft Audit Report, Army Healthcare Enterprise Management System (Project No. D2000CH-0108)

We have reviewed the subject draft report and enclosed are our comments.

Point of contact is Peter Langevin who can be reached at (703) 695-9423; email: langepb@hqda.army.mil.

Ernest J. Gregory
Deputy Assistant Secretary of the Army
(Financial Operations)

Enclosure

Printed on Recycled Paper

DRAFT OF A PROPOSED AUDIT REPORT

ARMY HEALTHCARE ENTERPRISE MANAGEMENT SYSTEM

Project No. D2000CH-0108 **September 11, 2000**

Recommendations:

A.1. We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller):

a. Investigate delivery order T0799BG0766 on contract GS-35F-4569G; delivery order T0799BG0799 on contract GS-35F-4076D; and delivery order T0799BG0745 on contract GS-35F-5404H for potential Antideficiency Act violations arising from the use of FY 1998 Army operation and maintenance funds to pay for EMS lease expenses in FYs 1999 and 2000 and the improper funding of a capital lease and labor cost for installation of a capital asset.

b. Comply with the reporting requirement of DoD Financial Management regulation 7000-14-R, "Administrative Control of Funds and Antideficiency Act Violations," if any violation of the Antideficiency Act occurred,

c. Provide a copy of the preliminary review report, the monthly status report on the formal investigation, and the final formal investigation report to the Inspector General, DoD.

Assistant Secretary of the Army (Financial Management and Comptroller).

Concur. A memorandum was sent to the Commander, U.S. Army Medical Command at Fort Sam Houston requesting he conduct an investigation to determine whether a potential Antideficiency Act violation occurred. Once we have received the preliminary report a copy will be forwarded to the Inspector General, DoD. If it is determined to be an Antideficiency Act violation, a copy of the final formal investigation will be forwarded to the Inspector General, DoD.

Audit Team Members

The Contract Management Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report. Personnel of the Office of the Inspector, DoD, who contributed to the report, are listed below.

Gerald E. Stephenson
Eric B. Edwards
Michael T. Hill
John R. Huddleston
Kimberly L. Ginn